

# COST PRINCIPLES FEDERAL & STATE GRANTS BASIC CONSIDERATIONS



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# Subpart E- Cost Principles

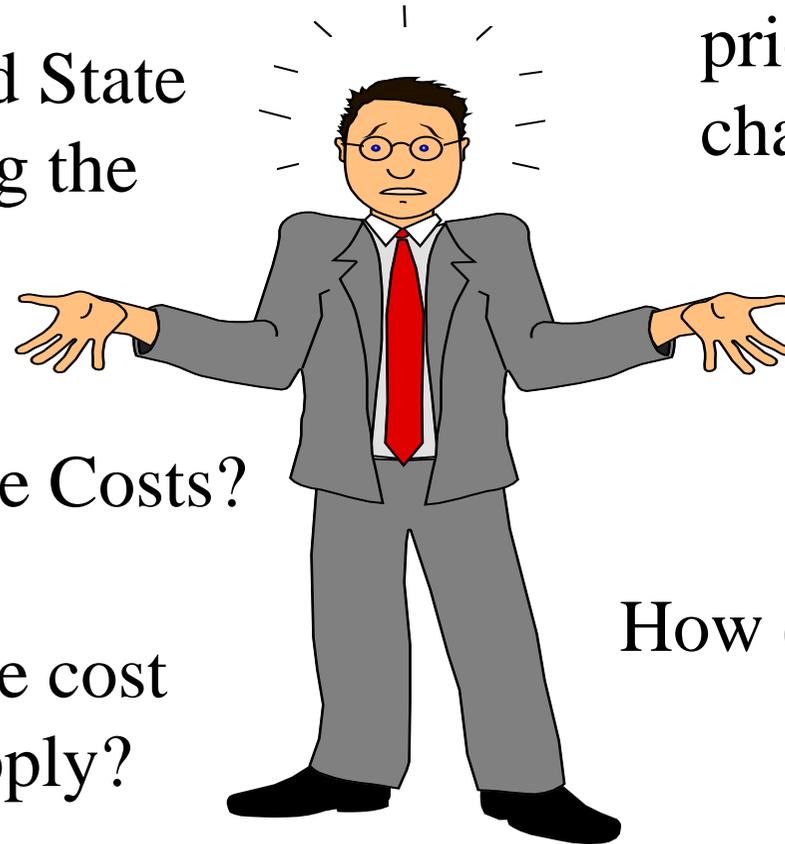
- ❖ **General Provisions § 200.400-.401**
- ❖ **Basic Considerations § 200.402-.411**
- ❖ **Direct & Indirect (F&A) costs § 200.412-.415**  
*Negotiated Indirect Cost Rate Agreements (additional training module)*
- ❖ **Special Considerations for States, Local Governments and Indian Tribes § 200.416-.417**
- ❖ **Special Considerations for Institutions of Higher Education § 200.418-.419**  
*General Provisions for Selected Items of Cost (next training module)*

# Why are Cost Principles Important?

What are the Federal and State requirements governing the funding received?

What are Reasonable Costs?

When do these cost principles apply?



When do I need prior approval to charge costs?

What are the fundamental premises?

How does this impact my organization?



## §200.400 Policy guide

The application of these cost principles is based on the fundamental premises that:

- a) The non-federal entity is responsible for the efficient and effective administration of the State, Federal and Federal pass-through award through the application of sound management practices.
- b) The non-federal entity assumes responsibility for administering State and Federal funds in a manner consistent with underlying agreements, program objectives, and the terms and conditions of the award.



## §200.400 Policy guide

The application of these cost principles is based on the fundamental premises that:

- c) Where wide variations exist in the treatment of a given cost item by the non-federal entity, the reasonableness and equity of such treatments should be fully considered.
- d) In reviewing, negotiating and approving cost allocation plans or indirect cost proposals, the cognizant agency for indirect costs should generally assure that the non-federal entity is applying these cost accounting principles on a consistent basis during their review and negotiation of indirect cost proposals.

# §200.400 Policy guide

The application of these cost principles is based on the fundamental premises that:

- e) The non-Federal entity may **not earn or keep any profit (increases in equity)** resulting from State or Federal financial assistance, unless explicitly expressly authorized by the terms and conditions of the Federal award



# §200.400 Policy Guide

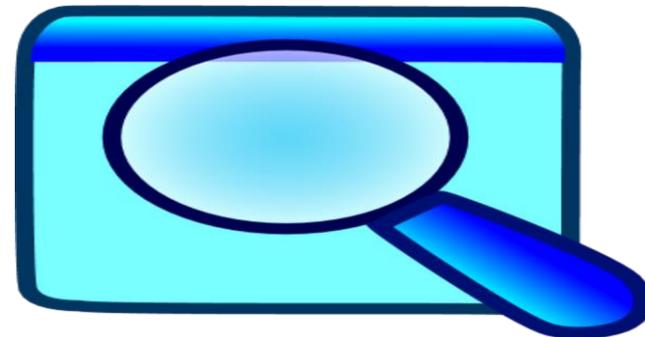
This language sets the tone for revised cost principles and emphasizes the implementation of a framework to better mitigate the risk of waste, fraud and abuse



# §200.401 Application

**General.** These principles must be used in determining the allowable costs of work performed by the non-federal entity under State, Federal and Federal pass-through awards.

These principles also must be used by the non-federal entity as a guide in the pricing of fixed-price contracts and subcontracts where costs are used in determining the appropriate price.





## §200.401 Application

The principles do not apply to:

- ❖ Arrangements under which State or Federal financing is in the form of loans, scholarships, fellowships, traineeships, or other fixed amounts based on such items as education allowance or published tuition rates and fees
- ❖ ***Fixed amount awards***. See also Subpart A—Acronyms and Definitions, §200.45 Fixed amount awards and §200.201 Use of grant agreements (including fixed amount awards), cooperative agreements, and contracts

# §200.401 Application

The principles do not apply to:

- ❖ *Federal Contracts.* Where a Federal contract awarded to a non-Federal entity is subject to the Cost Accounting Standards (CAS), it incorporates the applicable CAS clauses, Standards, and CAS administration requirements

CAS applies directly to the CAS-covered contract and the Cost Accounting Standards at 48 CFR parts 9904 or 9905 takes precedence over the cost principles in this Subpart E—Cost Principles of this part with respect to the allocation of costs.





## §200.401 Application

### The principles do not apply to:

- ❖ **Exemptions.** Some nonprofit organizations, because of their size and nature of operations, can be considered to be similar to for-profit entities for purpose of applicability of cost principles. Such nonprofit organizations must operate under Federal cost principles applicable to for-profit entities

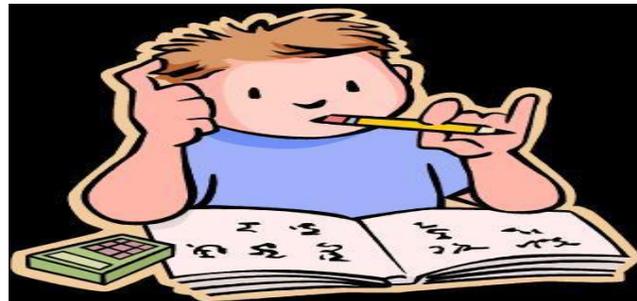
A listing of these organizations is contained in Appendix VIII to Part 200—Nonprofit Organizations Exempted From Subpart E—Cost Principles

# Basic Considerations

## §200.402 Composition of Costs

**Total cost**. The total cost of a Federal award is the sum of the allowable direct and allocable indirect costs less any applicable credits.

$$(\text{Direct} + \text{Indirect}) - \text{Credits} = \underline{\text{Total Cost}}$$





## §200.403 Factors affecting Allowability of Costs

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards:

- a) Be necessary and reasonable for the performance of the award and be allocable thereto under these principles.
- b) Conform to any limitations or exclusions set forth in these principles or in the award as to types or amount of cost items.
- c) Be consistent with policies and procedures that apply uniformly to both state and federally-financed and other activities of the non-federal entity



## §200.403 Factors affecting Allowability of Costs

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards:

- d) Be accorded consistent treatment. A cost may not be assigned to an award as a direct cost if any other cost incurred for the same purpose in like circumstances has been allocated to the award as an indirect cost.
- e) Be determined in accordance with generally accepted accounting principles (GAAP), except for state and local governments and Indian tribes, as otherwise provided for in this Part.

# §200.403 Factors affecting Allowability of Costs

Except where otherwise authorized by statute, costs must meet the following general criteria in order to be allowable under Federal awards:

- f) Not be included as a cost or used to meet cost sharing or matching requirements of any other federally-financed program in either the current or a prior period
- g) Be adequately documented

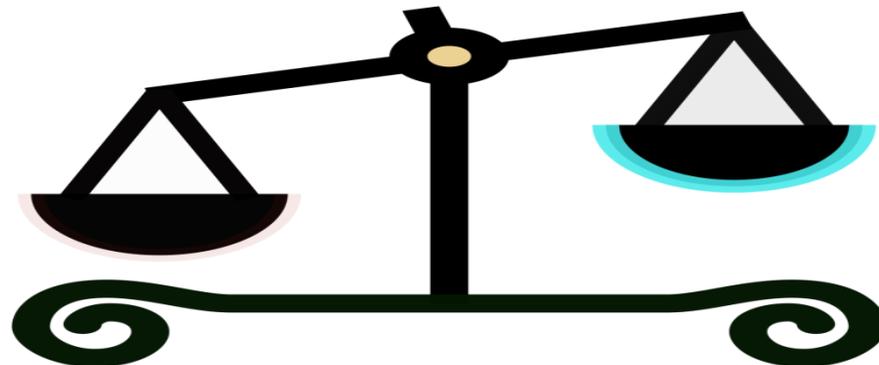
**CONSISTENCY**  
IS 

**KEEP  
CALM  
and  
FOLLOW  
THE RULES**

## §200.404 Reasonable costs

A cost is reasonable if, in its nature and amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the cost.

The question of reasonableness is particularly important when the non-Federal entity is predominantly federally-funded.





## §200.404 Reasonable costs

In determining reasonableness of a given cost, consideration must be given to:

- a) Whether the cost is generally recognized as ordinary and necessary for the operation of the non-federal entity or the proper and efficient performance of the award.
- b) The restraints or requirements imposed by such factors as: sound business practices; arm's-length bargaining; Federal, state, local, tribal, and other laws and regulations; and terms and conditions of the award.
- c) Market prices for comparable goods or services for the geographic area.

## §200.404 Reasonable costs

In determining reasonableness of a given cost, consideration must be given to:

- d) Whether the individuals concerned acted with prudence in the circumstances considering their responsibilities to the non-federal entity, its employees, where applicable its students or membership, the public at large, and the State and Federal government.
- e) Whether the non-federal entity significantly deviates from its established practices and policies regarding the incurrence of costs, which may unjustifiably increase the award's cost.





## §200.405 Allocable costs

- a) A cost is allocable to a particular award or other cost objective if the goods or services involved are chargeable or assignable to that award or cost objective in accordance with relative benefits received. This standard is met if the cost:
- ❖ Is incurred specifically for the award
  - ❖ Benefits both the award and other work of the non-federal entity and can be distributed in proportions that may be approximated using reasonable methods
  - ❖ Is necessary to the overall operation of the non-federal entity and is assignable in part to the award in accordance with the principles



## §200.405 Allocable costs

- b) All activities which benefit from the non-federal entity's indirect (F&A) cost, including unallowable activities and donated services by the non-federal entity or third parties, will receive an appropriate allocation of indirect costs.
- c) Any cost allocable to a particular Federal award under the principles provided for in this Part may not be charged to other Federal awards to overcome fund deficiencies, to avoid restrictions imposed by Federal statutes, regulations, or terms and conditions of the Federal awards, or for other reasons.
  - ❖ However, this prohibition would not preclude the non-Federal entity from shifting costs that are allowable under two or more Federal awards in accordance with existing Federal statutes, regulations, or the terms and conditions of the Federal awards.

## §200.405 Allocable costs

- d) Direct cost allocation principles. If a cost benefits two or more projects or activities in proportions that can be determined without undue effort or cost, the cost must should be allocated to the projects based on the proportional benefit.
- ❖ If a cost benefits two or more projects or activities in proportions that cannot be determined because of the interrelationship of the work involved, then, notwithstanding paragraph (c) of this section, the costs may be allocated or transferred to benefitted projects on any reasonable documented basis.
  - ❖ Where the purchase of equipment or other capital asset is specifically authorized under an award, the costs are assignable to the award regardless of the use that may be made of the equipment or other capital asset involved when no longer needed for the purpose for which it was originally required

## §200.405 Allocable costs

- e) If the contract is subject to Cost Accounting Standards, costs must be allocated to the contract pursuant to the CAS. To the extent that CAS is applicable, the allocation of costs in accordance with CAS takes precedence over the allocation provisions in this Part.





## §200.406 Applicable credits

- a) Applicable credits refer to those receipts or reduction-of-expenditure-type transactions that offset or reduce expense items allocable to the award as direct or indirect (F&A) costs.
- ❖ Examples of such transactions are: purchase discounts, rebates or allowances, recoveries or indemnities on losses, insurance refunds or rebates, and adjustments of overpayments or erroneous charges
  - ❖ To the extent that such credits accruing to or received by the non-federal entity relate to allowable costs, they must be credited to the award either as a cost reduction or cash refund, as appropriate

# §200.406 Applicable credits

- b) In some instances, the amounts received from the State and Federal government to finance activities or service operations of the non-federal entity must should be treated as applicable credits.
- ❖ Specifically, the concept of netting such credit items (including any amounts used to meet cost sharing or matching requirements) should be recognized in determining the rates or amounts to be charged to the award



## §200.407 Prior written approval

Under any given Federal, Federal pass-through or state award, the reasonableness and allocability of certain items of costs may be difficult to determine.

- ❖ To avoid subsequent disallowance or dispute based on unreasonableness or nonallocability, the non-federal entity may seek the prior written approval of the cognizant agency for indirect costs or the State and/or Federal awarding agency in advance of the incurrence of special or unusual costs
- ❖ Prior written approval should include the timeframe or scope of the agreement and must include the name and title of the individual from the granting agency



# §200.407 Prior written approval

- ❖ The absence of prior written approval on any element of cost will not, in itself, affect the reasonableness or allocability of that element, unless prior approval is specifically required for allowability as described under certain circumstances in the following sections of this Part:
  - (a) §200.201 Use of grant agreements (including fixed amount awards), cooperative agreements, and contracts, paragraph (b)(5);
  - (b) §200.306 Cost sharing or matching;
  - (c) §200.307 Program income;
  - (d) §200.308 Revision of budget and program plans;
  - (e) §200.311 Real property;



## §200.407 Prior written approval

- (f) §200.313 Equipment;
- (g) §200.332 Fixed amount subawards;
- (h) §200.413 Direct costs, paragraph (c);
- (i) §200.430 Compensation—personal services, paragraph (h);
- (j) §200.431 Compensation—fringe benefits;
- (k) §200.438 Entertainment costs;
- (l) §200.439 Equipment and other capital expenditures;
- (m) §200.440 Exchange rates;
- (n) §200.441 Fines, penalties, damages and other settlements;

# §200.407 Prior written approval

- (n) §200.441 Fines, penalties, damages and other settlements;
- (o) §200.442 Fund raising and investment management costs;
- (p) §200.445 Goods or services for personal use;
- (q) §200.447 Insurance and indemnification;
- (r) §200.454 Memberships, subscriptions, and professional activity costs, paragraph (c);
- (s) §200.455 Organization costs;



# §200.407 Prior written approval

- (t) §200.456 Participant support costs;
- (u) §200.458 Pre-award costs;
- (v) §200.462 Rearrangement and reconversion costs;
- (w) §200.467 Selling and marketing costs; and
- (x) §200.470 Taxes (including Value Added Tax); and
- (y) §200.474 Travel costs.



## §200.408 Limitation on allowance of costs

- ❖ The award may be subject to statutory requirements that limit the allowability of costs
- ❖ When the maximum amount allowable under a limitation is less than the total amount determined in accordance with the principles in this Part, the amount not recoverable under the award may not be charged to the award



# §200.409 Special Considerations

In addition to the basic considerations regarding the allowability of costs highlighted in this subtitle, other subtitles in this Part describe special considerations and requirements applicable to states, local governments, Indian tribes, and Institutions of Higher Education.





## §200.409 Special Considerations

Certain provisions among the items of cost in this subpart, are only applicable to certain types of non-Federal entities, as specified in the following sections:

- (a) Direct and Indirect (F&A) Costs (§§200.412 Classification of costs through 200.415 Required certifications) of this subpart;
- (b) Special Considerations for States, Local Governments and Indian Tribes (§§200.416 Cost allocation plans and indirect cost proposals and 200.417 Interagency service) of this subpart; and
- (c) Special Considerations for Institutions of Higher Education (§§200.418 Costs incurred by states and local governments and 200.419 Cost accounting standards and disclosure statement) of this subpart.

# §200.410 Collection of Unallowable Costs

Payments made for costs determined to be unallowable by either the Federal awarding agency, cognizant agency for indirect costs, or pass-through entity, either as direct or indirect costs, must be refunded (including interest) to the Federal government in accordance with instructions from the State or Federal agency that determined the costs are unallowable unless State or Federal statute or regulation directs otherwise.



# §200.411 Adjustment of Negotiated Indirect Cost Rate

## (containing unallowable costs)

- ❖ Negotiated indirect (F&A) cost rates based on a proposal later found to have included allowable costs must be appropriately readjusted by the cognizant agency
- ❖ These adjustments or refunds are designed to correct the proposals used to establish the rates and do not constitute a reopening of the rate negotiation. The adjustments or refunds will be made regardless of the type of rate negotiated





# Direct & Indirect (F&A) Costs

## §200.412 Classification of Costs

- ❖ There is no universal rule for classifying certain costs as either direct or indirect (F&A) under every accounting system
- ❖ A cost may be direct with respect to some specific service or function, but indirect with respect to the Federal award or other final cost objective
- ❖ Therefore, it is essential that each item of cost incurred for the same purpose be treated consistently in like circumstances either as a direct or an indirect (F&A) cost in order to avoid possible double-charging of Federal awards. Guidelines for determining direct and indirect (F&A) costs charged to Federal awards are provided in this subpart



## §200.414 Indirect (F&A) Costs

- ❖ Most organizations also incur costs for common or joint objectives that cannot be readily identified with an individual project or program
- ❖ Facilities operation and maintenance costs, depreciation, and administrative expenses are examples of costs that usually are treated as F&A costs
- ❖ The organization is responsible for the management and accounting of costs consistently and must not include costs associated with its F&A rate (Indirect Cost Rate) as direct costs

## §200.414 Indirect (F&A) Costs

2 CFR 200 explicitly requires pass-through entities (typically states and local governments receiving federal funding) and all federal agencies to reimburse the non-federal entity's indirect costs by applying the non-federal entity's federally negotiated indirect cost rate, if one already exists.

If a negotiated rate does not yet exist, then the non-federal entity is empowered either to:



- ❖ Request negotiating a rate with the Pass-through agency (State of Illinois)
- ❖ Elect the de minimis rate of 10 % of their modified total direct costs (MTDC)

# § 200.415 Required Certifications

To assure that expenditures and reports are proper and in accordance with the terms and conditions of the Federal/State award a required certification signed by an official who is authorized to legally bind the non-Federal entity is needed for:

- ❖ Approved and revised project budgets
- ❖ Annual and final fiscal reports
- ❖ Vouchers requesting payment under the agreements
- ❖ Indirect cost rate proposals
- ❖ Unallowable cost exclusion
- ❖ Lobbying



# Questions and Answers

Selected Items of Cost will be the next training module

